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EUR FOR MATT BRYZA  
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SUBJECT: ITALIAN ENERGY SUPPLIES PROJECTED TO BE ADEQUATE  
FOR WINTER 2006-2007

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SUMMARY  
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¶1. (U) Summary. Italian officials are optimistic Italy will not experience a repeat of last winter's energy shortages. Energy analysts point to a mild winter, gas reserves higher than last year, and Italy's increased ability to switch natural gas-fired power plants to oil. Looking past Italy's immediate energy needs, GOI officials and private sector analysts say Italy's long-term energy security should be increased by new agreements between Eni, Italy's oil and gas parastatal, and Gazprom, construction of at least two regasification plants in northern Italy and one in southern Italy, and the construction of additional natural gas pipelines connecting North Africa and the Caspian Basin to Italy. GOI officials support a coordinated EU energy policy to ensure long-term energy security for Italy and Europe. End summary.

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Italian Energy Supplies for Winter 2006-2007  
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¶2. (U) Italy, which generates over half of its electricity using natural gas, is better positioned to withstand increased winter demand for energy than last year, according to Giovanni Manfredi, the MFA office director-equivalent responsible for energy issues. Manfredi said that Italian energy companies have been increasing natural gas stocks since April to boost Italian natural gas reserves before winter. As a result, Manfredi noted that Italian strategic and working reserves are higher than at the beginning of last winter.

¶3. (U) Manfredi's optimism is consistent with that of Claudio Fava, Managing Director of Aquirente Unico, an Italian electricity reseller. Fava told Econoff that Italy will not experience power shortages similar to those of the winter of 2005-2006 because electricity companies are prepared to run natural-gas fired power plants using other energy sources. Fava also said Eni has notified its "preferred" customers they may have their gas supplies cut off in the event of a

nation-wide natural gas shortage. (Note: Preferred customers buy natural gas from Eni under long-term contracts with preferential pricing. In exchange for lower prices, preferred customers agree to have their natural gas supply cut under some circumstances. End note.)

14. (U) Diego Gavagnin, a former official at the Italian Energy Authority, now a private energy analyst, echoes Fava's optimism regarding energy supplies in the coming winter. In Gavagnin's view, Italian energy security has been enhanced by increased European dependence on Russian natural gas. Gavagnin's logic is that Gazprom will not run the risk of alienating European governments by cutting off natural gas flows, and will keep the gas flowing to ensure a steady income and increase Gazprom's share of the EU natural gas market. Gavagnin also predicted a mild winter in 2006-2007 will lower demand for natural gas and electricity used in heating.

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Italy's Long-Term Energy Security  
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15. (U) Manfredi acknowledged that Italy has been lucky with this year's mild winter and reduced demand for natural gas, but noted that in the long term, Italy needs a strategy to improve its energy security. All our interlocutors on energy issues say the GOI and Italy's energy industry are taking two approaches to improving energy security: increasing Italy's access to existing natural gas sources by constructing new natural gas pipelines and encouraging the formulation of a common EU energy policy.

16. (U) Italy currently imports roughly 30 percent of its natural gas supply from each of three sources: Russia, the North Sea, and Algeria. Natural gas pipelines connect Italy to natural gas fields in Russia, the North Sea, Algeria, and

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Libya. Italy plans to increase the capacity of existing pipelines and participate in the construction of new pipelines. Including pipelines currently under construction or in the planning phase, Italy will eventually be connected to natural gas fields by five pipelines: the Transgas pipeline, currently used to import Russian gas; pipelines connecting Italy to Norway; the Transmed and Green Stream pipelines connecting Italy to Algeria and Libya; the Turkey-Greece-Italy pipeline, which will bring Caspian natural gas to Italy; and the GALSI pipeline, which will connect Algeria to Sardinia and the Italian mainland. According to Manfredi, the GOI does not favor any one of these projects over another, but "supports any pipeline project that will bring natural gas to Italy." Manfredi said the GOI's long-term plan is to make Italy a natural gas hub for the Mediterranean, at the center of a "Mediterranean Ring" of natural gas pipelines.

Ties to Russia Improve Energy Security  
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17. (U) Eni, Italy's oil and gas parastatal, has continued to expand its presence in Russia through a closer relationship with Gazprom. In November 2006, Eni and Gazprom signed a cooperation agreement to develop each company's operations in the other's traditional market sector. The agreement will allow Gazprom to sell Russian gas directly to the Italian consumer. Gazprom's direct sales in Italy could reportedly reach three billion cubic meters annually by 2010. (Note: Italy consumes 80 billion cubic meters of natural gas annually. End note.) In exchange for giving Gazprom direct access to the Italian market, the agreement allows Eni to invest in gas exploration and extraction operations in Russia for sale to third parties, and leaves the door open to extending existing Gazprom contracts to supply gas to Italy through 2035.

¶8. (U) In addition to natural gas pipelines, ExxonMobil is building an LNG regasification terminal on Italy's Adriatic coast. BP has begun building a similar facility in Brindisi, but has had difficulty overcoming opposition from the local government, according to Manfredi. Eni has also recently announced it will construct an LNG plant in Southern Italy which could be operational within two-three years.

Power Plants in North Africa?

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¶9. (U) The GOI is considering supporting power plant construction in Algeria and Tunisia to generate electricity for export to Italy. It is unclear how this will increase Italian energy security, since the electricity would be generated using North African natural gas currently exported to Italy. Proponents of this plan, including Diego Gavagnin, a private sector energy consultant, and Claudio Fava, Managing Director of Aquirente Unico, note that this idea has the benefit of encouraging economic growth and development in the countries where the plants will be located, and of moving the greenhouse gas emissions out of Italy. Gavagnin pointed out that while these projects have not been economically feasible in the past, high oil and gas prices make them realistic. In contrast, the MFA's Manfredi is skeptical of the proposal to import electricity from Algeria and Tunisia, and noted that the electricity lines would have to connect with the Italian electricity grid in Sicily, which already has sufficient electricity-generating capacity. Additionally, if electricity generated in North Africa were to be shipped to the Italian mainland, it would have to be on electricity lines crossing the Strait of Messina, a geographic bottleneck, which Manfredi says is already over-crowded with power and other infrastructure.

Need to Press for EU Energy Policy

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¶10. (U) Manfredi said that in the long term, the GOI will seek to increase its energy security through the

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establishment of a common EU energy policy. He noted that progress towards a comprehensive, uniform, EU energy policy has been limited, due to the complex political and economic questions involved.

First Step: Integrate European Energy Grids/Pipelines

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¶11. (U) Absent an EU energy policy, Gavagnin made the case that further integration of the European energy grids will improve European, and Italian, energy security. He noted the European electricity grid is already partially integrated, and that electricity generated in Italy is sold to other EU countries. The next step, according to Gavagnin, is to establish of a Europe-wide spot-market for natural gas to allow cross-border natural gas sales on an as-needed basis. Gavagnin pointed out that a requirement for a Europe-wide spot-market for natural gas is an interconnected network of natural gas pipelines, which are currently being built on an ad hoc basis.

¶12. (U) Gavagnin also noted that European energy security can be enhanced by balancing European electricity generation among natural gas (concentrated in Italy), nuclear (France), coal (Germany), and renewable energy. Gavagnin estimated that natural gas, nuclear, and coal each account for 30 percent of Europe's electricity generation, with renewable energy making up the remaining ten percent.

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¶13. (U) One year after natural gas shortages caused the GOI to tap Italy's natural gas reserves and cut gas supplies to some customers, we are struck by differences in the two prongs of Italian energy security policy. On the one hand, the Italian energy industry is pursuing closer relations with Gazprom, with Eni entering into an agreement that will allow Gazprom to sell natural gas directly to Italian consumers in exchange for rights to invest in exploration and extraction opportunities in Russia. On the other hand, Italy seeks to distance itself from dependence on Russian natural gas through the construction or expansion of pipelines linking Italy to other natural gas sources. In this context, the pursuit of an EU energy policy can be seen as an attempt by the GOI to present a unified front to possible future efforts by Russia and other potential members (e.g., Algeria) of a "natural gas OPEC" to sell natural gas at a premium to European consumers.

¶14. (U) In fact, this dichotomy indicates to us the GOI continues to react to last year's energy crisis by pursuing all of the options at its disposal (increased access to Russian gas, building new pipelines to the Caucasuses and North Africa, and advocating for an EU energy policy) to ensure Italy's energy security. We expect the GOI to focus increasingly on the development of an EU energy policy, including Italy as a major producer of electricity using natural gas. End comment.  
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